

Investor Insights

JUNE 2025 QUARTER



In summary

Global financial markets showed notable resilience in the second quarter of 2025, with several major equity indices, including the ASX, reaching record highs despite persistent policy uncertainty and market volatility. Sentiment was initially shaken by the Trump administration's unexpectedly aggressive tariff announcements, triggering a sharp selloff. However, markets rebounded as many of these measures were delayed or renegotiated, restoring confidence and supporting a rotation back into equities.

Despite elevated geopolitical risks, equities continued to rise, buoyed by better-than-expected corporate earnings, forward guidance, and strong interest in structural themes such as artificial intelligence and defence spending. Bond markets remained volatile, balancing the effects of higher fiscal spending and rising debt issuance with the inflationary implications of trade policy and slowing economic momentum.



In this edition

We explore key developments across global markets and what they might mean for investors going forward:

- Easing inflation pressures have allowed the Reserve Bank of Australia (RBA) to reduce the cash rate, but despite a recent pause, **a further three rate cuts are expected.**
- Currently, **there are significantly more global central banks cutting interest rates than hiking.** This broad-based monetary policy easing should provide substantial support to the global economy. Equity and bond markets, particularly in regions where interest rate cuts are on a more aggressive path, also stand to benefit.
- Investors often hesitate to invest in equity markets at all-time highs, but historical data shows that **returns following market highs are frequently stronger than average.**
- **The Commonwealth Bank (CBA) share price has experienced a strong run;** however, a comparison to global peers highlights why analysts remain bearish on the share price.
- Gold has decoupled from its historical interest rate relationship since Russian central bank assets were confiscated in 2022. **Global central banks have subsequently increased their gold holdings,** which has helped push the price of the yellow metal higher in a trend that is likely to continue.
- **Equity markets have recouped the “Liberation Day” selloff and reached new highs.** While several factors support the equity market outlook, downside risks remain due to ongoing economic and trade uncertainty.

Global markets brush off uncertainty, but economic risks remain

Global financial markets have enjoyed stronger than expected performance despite rising economic risks. In the US, sentiment data has softened, but core indicators like employment and output remain relatively resilient and signal only a marginal slowdown rather than a significant reduction in economic activity.

Australian economic growth remains anemic; however a more favourable policy backdrop characterised by subdued inflation, fiscal support, and rate cuts should help support economic activity. Global monetary policy is expected to support financial markets and the global economy in the face of weakening economic conditions.

The most likely base case for the global economy under these conditions is a **'Slower Economic Growth'** scenario.

This scenario involves US tariffs being broadly implemented, with a moderate portion subject to renegotiation, leaving base tariffs of at least 10% in effect. This environment

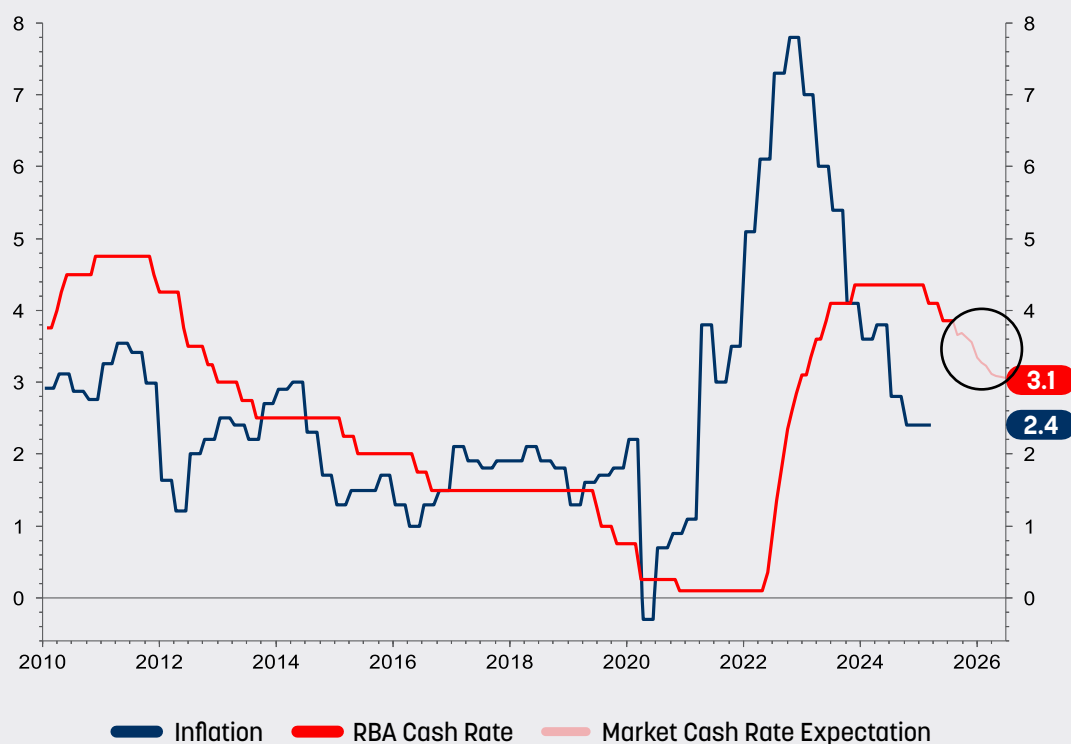
is expected to lead to a slowdown in global economic growth. Inflation is projected to rise temporarily due to the tariffs; however, slowing economic growth and an increase in unemployment should prompt further interest rate cuts from central banks to support growth.

Bond markets will likely remain range bound, balancing the risks of higher inflation with a weakening economic growth outlook. Outside of tariff-affected sectors, corporate earnings growth is anticipated to stabilise and remain positive, with potential for upside surprises. Elevated valuations may, however, make equity markets vulnerable to disappointing earnings results.

Markets price lower rates for Australia as inflation slows

Australia's headline Consumer Price Index (CPI) has trended down and now remains within the RBA's 2-3% inflation target range. Chart 1 illustrates this slowdown in inflation (blue line), with the latest quarterly CPI reading of 2.4% year-on-year positioning it at the lower end of the downtrend.

Chart 1: Australian inflation and cash rate expectations - more rate cuts expected in the next 12 months



Source: LSEG Datastream, Quilla Consulting

Recent data also suggests some stickier components, like new dwelling prices, rents and insurance premiums, are also showing further moderation, pointing to lower future inflationary pressure. The slowdown in inflation does not mean that prices have reverted to historical levels and that costs have gone down, rather that the pace of price rises has slowed sufficiently for the RBA to consider reducing the cash rate.

The current inflation dynamics are a positive sign for the future direction of interest rates. The cash rate (see red line in Chart 1 on the previous page) has begun to fall after two 0.25% cuts by the RBA in February and May this year. Economists had expected the RBA to deliver another rate cut in early July, but the RBA opted to delay this action, waiting on further evidence that inflation will sustainably remain within its target range.

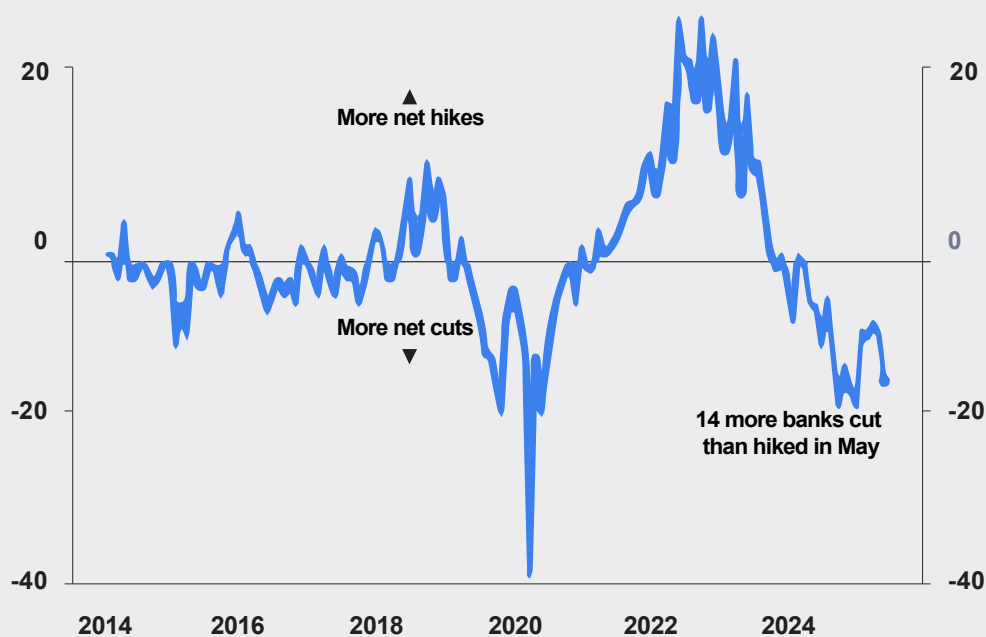
Current expectations are that the RBA will proceed with another rate cut in August, post the June quarter CPI data release. Market expectations (see light red line in Chart 1 on the previous page) indicate that the cash rate is expected to decrease by approximately 80 basis points to just above 3% over the next 12 months.

The domestic economy will be supported by interest rate cuts. For investors, the returns on cash and term deposits are set to fall, while declining interest rates will be positive for bond prices. Equity markets are also expected to be supported in a falling interest rate environment.

Synchronised global monetary policy easing

Currently, there are more global central banks cutting interest rates than hiking rates globally. The difference between the number of central banks cutting versus hiking rates is currently near the highest level seen in the past decade, excluding the Covid-19 period (Chart 2).

Chart 2: The balance of rate hikes and cuts from 52 global central banks



Source: Bloomberg Opinion

This broad-based monetary policy easing is expected to provide a boost to the global economy through the supportive effects that lower interest rates should have on both consumers and businesses. Lower policy rates also reduce the discount rates used in investment decision making, which will be supportive of equity market valuations.

As the world's largest economy, the US has already provided economic support through interest rate cuts. However, these cuts have

been slower than anticipated due to the uncertain impact of tariffs on both US inflation and growth. The US Federal Funds Rate is projected to decline by 100 basis points over the next 12 months, reaching a target range of 3.25% to 3.5%. This should support both US and global economic growth.

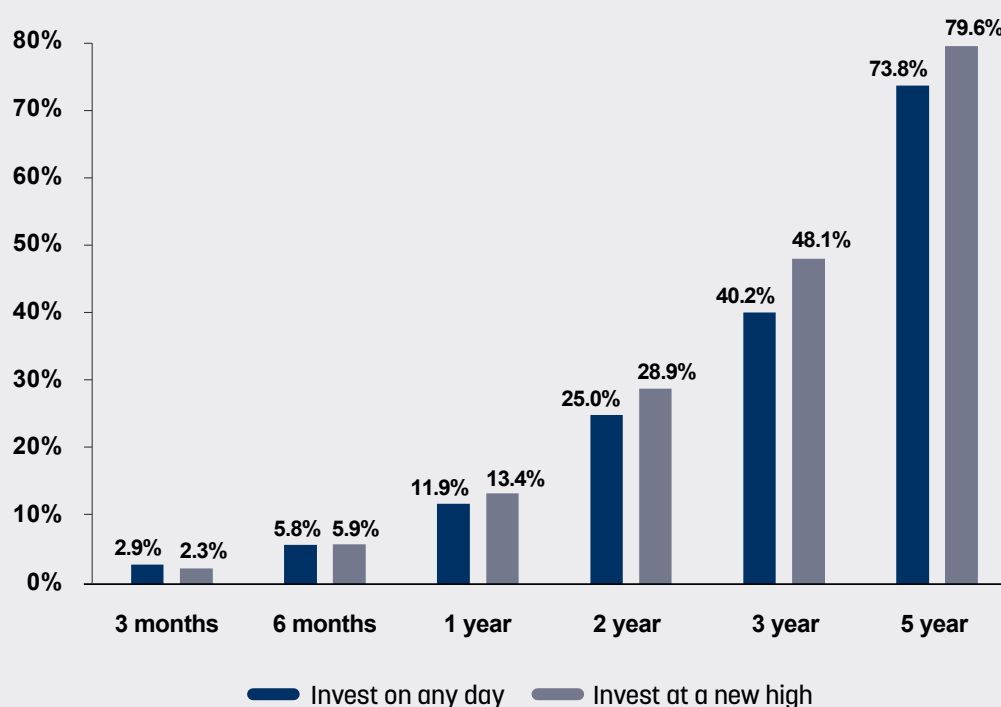
This supportive monetary policy environment is likely to benefit financial markets, especially economically and interest rate-sensitive sectors.

Investing at all-time highs

As many global equity markets, including Australian equities, make new all-time highs, investors often experience reservations about the outlook for future returns, particularly amid economic uncertainty and recent market volatility.

Chart 3 illustrates the performance of the US equity market (S&P 500 Index) following investments made at new all-time highs. It then compares these returns to the market's average returns over the same periods. The data suggest that, generally, investing at all-time highs should not be a cause for concern and that returns following new highs have often been stronger than average.

Chart 3: Average cumulative total returns when investing on any day vs at new highs S&P500: 1988-2023



Source: JP Morgan Asset Management

"Invest on any day" represents the average of forward returns for the entire time period, whereas "Invest at a new high" represents the average of rolling forward returns calculated from each new S&P 500 high for the subsequent 3-M, 6-M, 1-Y, 2-Y and 3-Y intervals.

New highs generally indicate robust underlying market drivers that propel equity returns, even if these factors aren't immediately obvious. Historically, investing at new highs has not increased the risk of poor returns or signaled an imminent reversal. Instead, it often coincides with periods of positive momentum, as strong price trends tend to persist.



Commonwealth Bank: comparative insights to global giants

The strong performance of Commonwealth Bank (CBA) has lifted its market capitalisation above \$300bn at recent highs, with CBA now representing approximately 11.5% of the Australian equity market (ASX200 Index). Its strong performance and large weighting have helped drive the performance of the overall market.

Active Australian fund managers have largely remained underweight in their portfolio allocations, which has caused underperformance as CBA's price pushed ever higher. Market analysts are also bearish on the share price, with most analysts that cover CBA issuing sell recommendations (0 buys, 2 holds, 14 sells). This bearishness is not reflective of the quality of CBA as a business but rather represents concerns around its valuation given a modest earnings and revenue growth outlook.

Comparing CBA to JP Morgan (world's largest bank) and Nvidia (world's largest company) in Table 1 provides further insights:

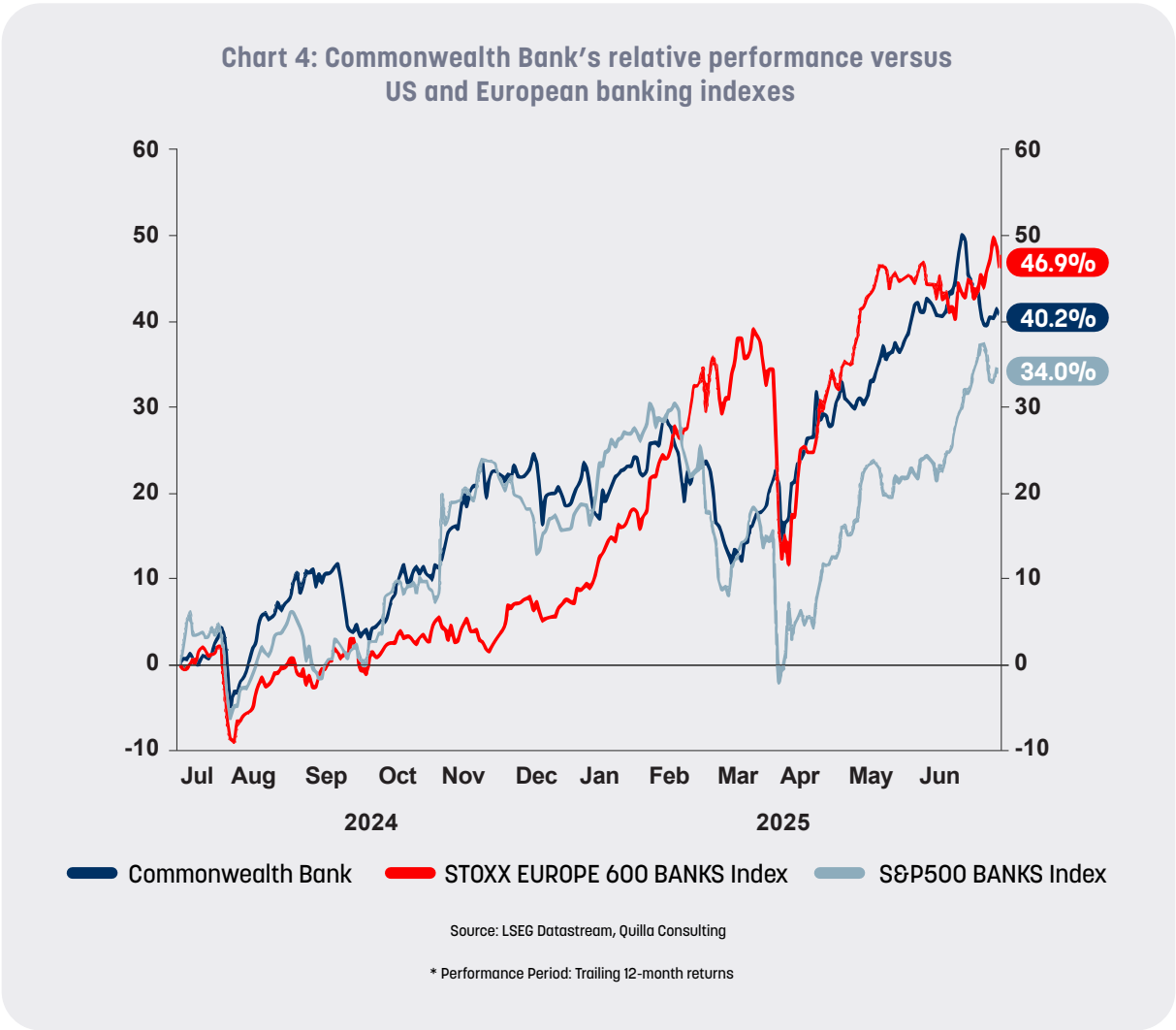
- Share price performance: CBA has broadly tracked the performance of global banks over the past year and outperformed Artificial Intelligence (AI) powerhouse Nvidia.
- Revenue and earnings growth: CBA's forward revenue and earnings growth are both modest, similar to JP Morgan, but far below those of Nvidia.
- Valuation: CBA trades at a forward Price to Earnings Ratio (P/E) of 29x (P/E refers to the price an investor pays per dollar of earnings). This is almost double that of JP Morgan and close to Nvidia's, while delivering lower returns on equity.

Table 1: Commonwealth Bank vs Nvidia vs JP Morgan

	Forward Price to Earnings	Forward Revenue Growth (%)	Forward Earnings Per Share Growth (%)	Forward Return on Equity (%)	YTD Performance (%)	1Y Performance (%)
NVIDIA (largest company by market cap)	36.7	53.7	44.9	79.4	14.2	22.6
JP Morgan (largest global bank)	16.0	-1.8	1.5	15.6	22.6	43.2
Commonwealth Bank	28.7	2.5	2.6	13.5	20.8	51.2

* Performance data at as 1 July 2025 | Source: LSEG; Bloomberg LP

While many theories attempt to explain CBA's performance, a comparison with US and European banks (Chart 4) reveals a broader common trend of positive investor sentiment toward the banking sector globally. This has attracted significant capital, elevating the sector globally.

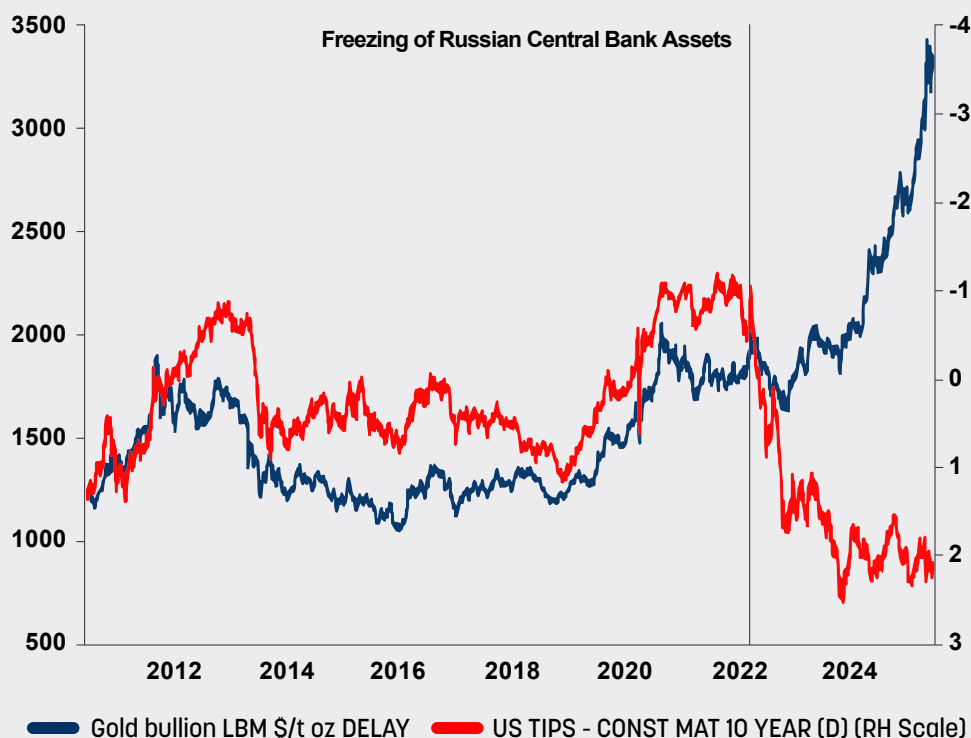


Company valuations can remain elevated for prolonged periods of time, and a high valuation is not necessarily a signal that a company's share price will fall in the near term. The outlook for CBA as a business is fundamentally sound, but the current valuation and recent performance may indicate that future returns could disappoint.

Gold decouples from real interest rates as central banks lift demand

Gold has been a standout investment over the last few years. Its performance has, however, deviated from fundamental relationships that drove gold demand in the past. Historically, gold's appeal is inversely related to real interest rates (nominal interest rates minus inflation). This fundamental relationship has decoupled since 2022, shown in Chart 5, following the G7's freeze of over \$280 billion in Russian central bank assets after the Ukraine invasion.

Chart 5: Gold versus real US interest rates (inverse scale) - decoupling since Russian assets were frozen



Source: LSEG Datastream, Quilla Consulting

Central banks have responded by buying more gold to increase the portion of their reserves that remain out of reach of potential confiscation. Goldman Sachs research indicates a fivefold increase in central bank gold purchases on the London Over the Counter (OTC) market since 2022.

Emerging market central banks are also notably increasing their gold reserves, narrowing the gap with developed economies. For instance, China holds 6.5% of its reserves in gold and India 13.5%, compared to over 70% for the US, Germany, France, and Italy, which remain high as a legacy of the gold standard.

Investor demand for gold has also notably increased more recently, evident by strong flows into gold Exchange Traded Funds (ETFs). Central bank purchases are, however, more stable and consistent buyers of gold with less sensitivity to market fundamentals and price moves.

The trend of central bank buying is likely to continue, and while we have a constructive outlook for gold, we are mindful of potential short-term volatility.

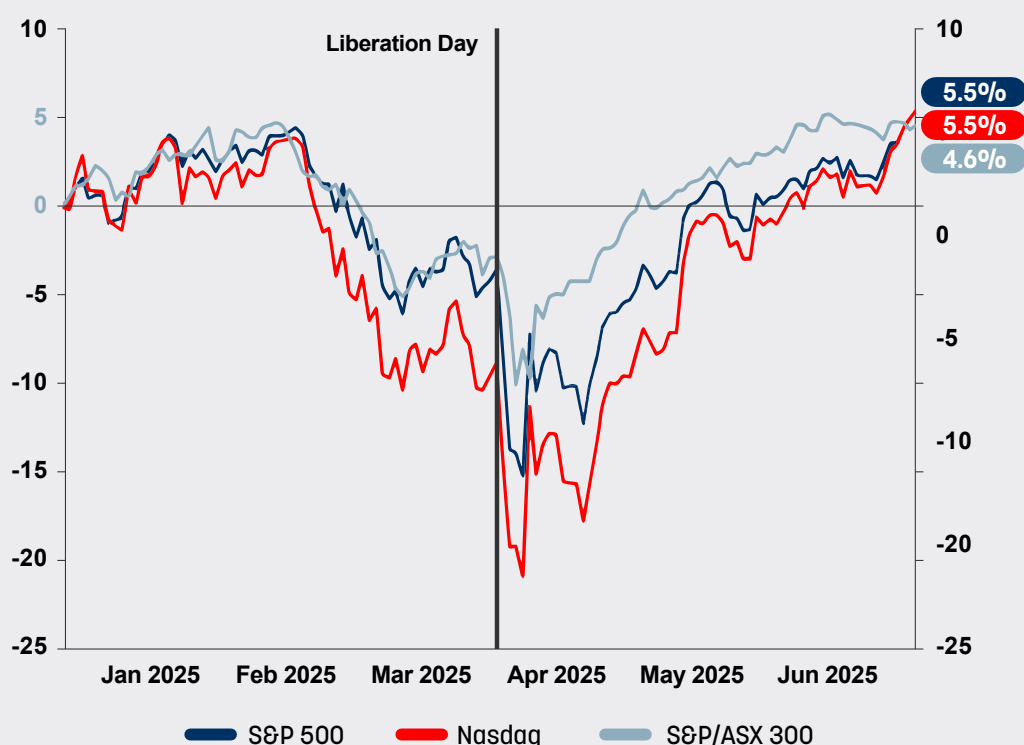
Liberation day sell-off recouped and new highs – what now?

Global equity markets experienced a spike in volatility in April, ignited by the Trump administration's announcement of a broad array of reciprocal tariffs that were higher than markets had originally anticipated. The so called "Liberation Day" tariffs led to a substantial market sell off.

However, global equity markets staged sharp recoveries and ended the quarter well above preannouncement levels as it became evident that the Trump administration was willing to reduce the level of tariffs and delay their implementation.

As illustrated in Chart 6, the Australian equity market (ASX300 Index) saw a less pronounced drawdown, falling 13% from its February all-time highs. In contrast, the broader US equity market (S&P500 Index), fell 19%, while the mega-cap technology-heavy Nasdaq Index experienced a 24% drawdown.

**Chart 6: Australian and US equity market performance
1 January – 30 June 2025**



Source: LSEG Datastream, Quilla Consulting

Equity markets have not only rebounded from the “Liberation Day” selloffs but are currently positive for the year-to-date and trading near all-time highs.

The direction of equity markets from here will depend on several evolving factors:

- Continuation of the rally: sustained gains depend on steady economic data, constructive trade developments, and further progress on pro-growth government policies and fiscal stimulus.
- Trade dynamics and economic impact: while the conclusion of major trade deals appears likely, the adverse effects generated by past disruptions will likely persist. Tariffs are set to be applied in varying degrees, which is expected to act as a headwind for US growth, market sentiment, and earnings in select sectors.
- Corporate earnings: expectations for earnings growth have been notably downgraded since the start of 2025.

Entering the US earnings season with subdued expectations increases the chance for upside surprises, however, elevated valuations increase the risk that disappointing results will trigger sharp negative market reactions.

- Sector leadership: large-cap technology companies are expected to remain resilient amid ongoing macro uncertainty. Their defensive attributes are underpinned by secular growth trends such as artificial intelligence.
- Easing monetary policy: central bank rate cuts should provide continued support for equity markets globally.

While the current environment presents several supportive factors for global equities, persistent risks across the economic, trade, and corporate earnings landscape warrant continued vigilance.

Outlook

As we enter the second half of 2025, we maintain a moderately constructive outlook for global growth and equity market performance. However, volatility is expected to persist amid competing policy forces in the US, where President Trump's mix of protectionist trade measures and fiscal stimulus continues to unsettle markets.

US earnings estimates have stabilised, and downbeat expectations increase the potential for upside surprises, however elevated valuations could make equities vulnerable to earnings disappointments. Europe may continue to benefit from rising fiscal support, while Australian equities

face headwinds from modest earnings growth and relatively high valuations.

Meanwhile, global rate-cutting cycles are underway, with Australia likely to deliver multiple cuts amid subdued private demand and easing inflation. This global monetary policy easing is expected to support economic activity, consumer confidence, and investor sentiment.

Despite potential risks, structural themes and accommodative policy stances should support global financial markets. Navigating these dynamic markets will require a disciplined approach focusing on diversification, active market monitoring, and tactical flexibility.